NTERNATIONAL/FOREIGN TRADE

International trade refers to trade between countries i.e. it is the exchange of goods and services between two or more countries. International trade involves:

(a) **Import trade;** this is the buying of goods and services from other countries. Traders who buy goods from other countries are called importers and the goods and services bought from other countries are called imports. Uganda's imports include medicine, clothes, machinery, vehicles etc.

(b) **Export trade;** this is the selling of goods and services to other countries. Traders who sell goods to other countries are called exporters and the goods and services sold to other countries are called exports. Uganda's exports include coffee, fish, flowers, tourism etc.

(c) **Entrepot trade;** this is the re-exportation of previously imported goods. For instance, a trader may import vehicles from Japan hoping to sell them in Uganda but later re-export the vehicles to Rwanda. It may also happen that a producer imports raw materials from abroad and later export the finished goods made from the imported raw materials.

WHY DOES INTERNATIONAL TRADE ARISE?

(a) **Differences in climates;** different countries have got different climatic conditions. For instance, while one crop may do well in one country, it may not do so in other countries.

(b) **Differences in resource endowment;** nature has blessed different counties with different natural resources such as minerals, lakes, mountains, rivers, forests etc.

(c) **Differences in skills;** developing countries have less industrial skills and therefore tend to concentrate in the production of raw materials, which they exchange to get finished products from developed industrialized countries.

(d) **Differences in costs of production;** some countries produce certain products at lower costs compared to other countries (comparative

advantage). So countries will tend to concentrate in the production of those commodities where they have got comparative advantage.

(e) No single country can produce all the goods and services needed by her people. So countries need to trade with other countries in order to obtain the goods and services they are unable to produce.

(f) **Surplus production;** some countries produce certain commodities in excess of home consumption and therefore need to sell off the excess instead of leaving it to be wasted.

(g) **Specialisation;** countries tend to concentrate in the production of those commodities where they have got an advantage over other countries and then exchange to get what they do not produce.

TERMS USED IN INTERNATIONAL TRADE

1. **Bi-lateral trade;** this is where exchange of goods and services is in between two countries only e.g. if Uganda imports goods from Kenya and exports goods to Kenya only.
2. **Multi-lateral trade;** this is where exchange of goods and services is in between many countries (Three and more) e.g. if Uganda trades with Japan, Kenya, Rwanda, China etc.
3. **Visible trade;** this refers to importation and exportation of goods only (tangible things) e.g. motor vehicles, coffee, flowers etc. Visible imports refer to imported goods while visible exports refer to exported goods.
4. **Invisible trade;** this refers to the importation and exportation of services only e.g. tourism, insurance, banking etc.
5. **Balance of trade/Balance of visible trade;** this is the difference between visible imports and visible exports. It is a record of the overall flow of physical goods between countries. When a country's visible exports exceed its visible imports, the country is said to be experiencing a favorable balance of trade. When the visible imports exceed the visible exports, the country is said to be experiencing an unfavorable balance of trade.
6. **Terms of trade;** this is the relationship between export prices and import prices. If the prices of exports are higher than those of imports,

a country is said to be experiencing favorable terms of trade. But if the prices of imports are higher than those of exports, a country is said to be experiencing unfavorable terms of trade.

7. **Rate of exchange;** this is the price of one currency in terms of another currency. The exchange rate is determined by both government and forces of demand and supply.
8. **Balance of payments (on current account);** this is the difference between a country's receipts from exports (both visible and invisible) and payments for imports (both visible and invisible). If a countries receipts from exports exceed payments for imports, the country is said to be experiencing a favorable balance of payments. But if the payments for imports exceed receipts from exports, the country is said to be experiencing unfavorable balance of payments (balance of payments deficit). In addition to payments for imports, a country may invest money in other countries by either loaning money or establishing industries in those countries. Such expenditure is termed capital expenditure. At the same time, a country may receive money from other countries in form of investments or loan and such receipts are termed capital receipts. The difference between capital receipts and capital expenditures is called balance of payments on capital account. The difference between receipts and payments on both current and capital accounts is called the overall balance of payments.

HOW TO CORRECT A BALANCE OF PAYMENTS DEFICIT

1. Increasing exports; this increases the amount of money received from exports.
2. Reducing imports; this reduces the amount of money paid out for imports.
3. Encouraging foreign investors in the country; this increases the amount of capital receipts and also increases domestic output which may be exported.
4. Increasing taxes of imported goods in order to discourage importation hence reducing outflow of foreign exchange.

5. Giving subsidies to local producers in order to increase domestic production hence reducing imports and increasing exports.
6. Diversification of exports; producing different goods for export hence increases inflow of foreign exchange.
7. Currency devaluation; thereby encouraging exportation and discouraging importation.

ADVANTAGES OF INTERNATIONAL TRADE

1. International trade enables a country to obtain the goods and services she cannot produce herself from other countries.
2. It also enables a country to dispose off her surplus goods which would otherwise have been destroyed due to limited local market.
3. International trade enables citizens of a country to get a variety of goods and service, both locally produced and imported hence improving their standard of living.
4. International trade creates healthy competition between local and foreign producers leading to the production of better quality products and reduced prices.
5. International trade promotes international peace and understanding among countries. For instance, a country would not like to go to war against a trading partner.
6. International trade encourages specialization among different countries resulting in increased output and quality products.
7. International trade enables a country to cope with effects of natural calamities such as drought, floods etc. When a country has not been able to produce and provide basic necessities because of natural calamities, supplies can be obtained from other countries.
8. International trade is a source of revenue to government through the taxes charged on imports and exports.
9. Export trade brings in foreign exchange, which is needed for a country to buy goods and services from other countries.
10. International trade provide employment opportunities to people involved in importing, exporting, transporting, clearing and forwarding etc.

11. Through international trade, local producers are able to get advanced skills from developed industrialized countries leading to increased output and improved quality.

DISADVANTAGES OF INTERNATIONAL TRADE

1. Goods imported from developed industrialized countries a threat to local infant industries i.e. reduce demand for locally produced goods.
2. Export trade may lead to exhaustion of some resources as a result of over exploitation e.g. over fishing.
3. It may result in importation of defective goods (expired or poor-quality goods) which end up affecting the health of the citizen.
4. International trade encourages dumping. Dumping is the sale of goods in a foreign market at a price lower than what is charged in the home market. The problem of dumping is that it reduced market for locally produced goods in those countries where the goods are sold cheaply.
5. Some of the goods imported may have adverse effects on people's morals e.g. romantic literature (blue movies).
6. International trade may lead to over dependence. In case of wars or political misunderstandings, a country may suffer shortage of essential goods and services.
7. Excessive importation may result in a country suffering from unfavorable balance of payments.
8. International trade widens the gap between developed countries and developing countries. It makes rich countries richer and poor countries poorer because of unfavorable terms of trade.
9. Import trade may bring about imported inflation if goods are imported from countries suffering from inflation.

TERMS OF SALE (PRICE QUOTATIONS) IN INTERNATIONAL TRADE

A lot of expenses are involved in international trade e.g. loading charges, import/export duties, freight charges, insurance charges, dock handling charges and dock dues etc. Some of these expenses may be paid by the exporter and therefore included in the price quoted to the buyer, while others may be paid separately by the buyer himself. The exporter should therefore indicate what expenses have been included in the price quoted and what expenses are to be paid by the buyer himself. The following terms are used in Quotations and Invoices to show this position clearly.

1. Ex-works/Ex-factory/Ex-stock/Ex-warehouse; this price quotation covers only the cost of the goods as they leave the seller's factory/premises and all the other expenses have to be paid by the buyer separately. This is the lowest price quoted.
2. Free on rail (FOR); this price quotation includes the cost of the goods plus cost of carriage to the nearest railway station from the seller's factory. All other expenses have to be paid by the buyer separately.
3. Delivered Docks (DD); this price quotation includes the cost of the goods and cost of carriage up to the docks. Docks are places at the port where ships wait for cargo.
4. Free alongside ship (FAS); this price quotation includes the cost of the goods, cost of carriage up to the docks plus dock handling charges and dock dues but does not include loading the goods onto the ship.
5. Free on board (FOB); this price quotation includes the cost of the goods and all charges up to the point of loading the goods onto the ship but does not include freight by ship.
6. Cost and Freight (C & F); this price quotation includes the cost of the goods and all charges up to the port of destination but does not include insurance charges.
7. Cost, Insurance and Freight (CIF); this price quotation includes the cost of the goods and all charges up to the port of destination including insurance charges (Marine insurance).

8. Loaded; this price quotation includes the cost of the goods and all charges up to the port of destination plus unloading charges.
9. In Bond; this price quotation includes the cost of the goods and all charges up to when goods are delivered to a bonded warehouse, including warehouse handling charges.
10. Duty paid; this price quotation includes the cost of the goods and all charges until the goods reach a bonded warehouse plus any customs duty payable.
11. Free of expenses (Franco); this price quotation includes the cost of the goods and all charges until the goods reach the buyer's premises i.e. there are no any other expenses to be paid by the buyer separately. It includes:
    a. Cost of the goods,
    b. Freight charges,
    c. Insurance charges,
    d. Handling charges,
    e. Customs duties,
    f. Dock dues.

DOCUMENTS USED IN INTERNATIONAL TRADE

1. Indent; this is a request by the importer to his agent, to place an order for goods on the behalf of the importer. It shows the details of the goods required by the importer. An indent may either be open or closed. An open indent one in which the importer does not specify the supplier from whom the agent is to order the goods i.e. the agent is free to choose the supplier he thinks most appropriate. A closed indent is one in which the importer states the importer from whom his agent is to order the goods.
2. Certificate of origin; this is a document which specifies the country from where the imported goods are originating from to enable customs authorities to calculate the customs duty correctly. This is because many countries enter into trade agreements thereby agree to charge no or low customs duties on goods or services originating from each other.
3. Consular invoice; this is an invoice that has been seen and signed by the consulate (embassy) of the importing country stationed in the exporting country. That is to ensure that goods are reasonably prices and that no

undesirable goods are dispatched to the importing country. A consul/ambassador is an official appointed by a state to live in a foreign country to protect the interests of its citizens.

4. Bill of lading; this is a contract of carriage between the shipper or consignor (sender of the goods) and the shipping company. It is signed by the captain of the ship as evidence of receipt of goods by the shipping company from the shipper for transportation.

   Contents of a bill of lading:

   a. The name of the shipping company.
   b. The name of the shipper or consignor (sender of the goods).
   c. The name of the consignee (person to who the goods are being sent)
   d. The details of the goods loaded unto the shipper.
   e. Terms and conditions under which the shipping company has accepted the goods.

   NB: Goods accepted on the ship while damaged get a dirty bill. Otherwise goods have to be received while in good condition to get a clean bill.

   A bill of lading has got three functions:

   i. It is evidence of receipt of goods by the shipping company.
   ii. It is a contract of carriage i.e. it shows the terms and conditions under which the goods have been accepted for shipping.
   iii. It is a document of title to the goods i.e. a person named on this document can claim for the goods.

   NB: The seller/exporter/shipper/consignor sends a copy of a bill of lading to the buyer/importer/consignee, to enable him receive the goods when the ship reaches the port of destination.

5. Letter of credit; is a guarantee/assurance by the issuing bank to pay a sum of money to the exporter on behalf of the importer in the event that the importer does not pay the exporter. When an importer wants to buy goods on credit, the exporter may ask the importer to open a letter of a credit in the exporter's favor with a reputable bank in the exporter's country. The importer approaches his bank which issues a letter of credit with a reputable bank in the exporter's country. The importer's bank is called the issuing bank while the bank in the exporter's country is called

the corresponding bank. A letter of credit may either be revocable or irrevocable. A revocable letter of credit is one which can be withdrawn or its terms changed by the importer without prior consent of the exporter. An irrevocable letter of credit on the other hand is one which cannot be withdrawn or modified in any was without the permission of the exporter. A further measure of safety is for the exporter to ask for a confirmed irrevocable letter of credit, which is guaranteed by both the issuing bank and the corresponding bank.

6. Letter of hypothecation; this is a written agreement by which the exporter authorizes the bank or lender to sell or repossess the pledged goods/item in case it cannot obtain payment from the importer. This happens if the bank cannot obtain payment on a bill of exchange drawn on the importer that has been already discounted for the exporter. Should the bank receive less money from the sale of goods, the deficit is made up by the exporter and likewise any surplus from the sale is remitted to the exporter.
7. Proforma Invoice; is a document sent by the seller/exporter to the buyer/ Importer in advance of deliver of goods, to show how the actual invoice would look like if goods are actually sent. It is usually sent if payment is expected before delivery. It enables the buyer/importer to obtain necessary permissions from the central bank or to sort out customs formalities.
8. Charter party; this is a deed/contract between a shipowner and a trader (charterer) for the hire of a ship. It gives the charterer absolute control over the ship for the period of contract or charter. A trader may hire the entire ship if he has enough to fill the ship. Charter parties are two kinds:
    a. Time Charter; this is when a charterer hires the ship for a certain period of time, say for three months.
    b. Voyage charter; this is when a charterer hires the ship for a certain voyage/journey.
9. Ship's manifest; this is a customs declaration giving full details of the contents of the ship i.e. details of the crew, passengers and cargo carried. It is presented to the customs office as soon as the ship arrives at the port of destination before the ship is unloaded.

10. Dock Warrant; this is a document issued to the dock authorities to the trader whose goods are being held at the dock. If the goods are sold while at the dock, the seller transfers the dock warrant to the buyer to enable the buyer claim for the goods.
11. Calling Forward Note; this is a document issued by the shipping company to the shipper/exporter informing him of the date and time by which goods should be at the dock ready for loading unto a particular ship.
12. Shipping Note; this is a document that gives details of goods being shipped by sea. It is addressed by the shipper to the captain of the shipper, requesting him to receive on board specified goods and a receipt for the mate to sign. A document accompanying goods when they are sent to docks for export.
13. Airway bill; this is a contract of carriage between the trader/exporter and the airline company for goods transported by air. An Airway Bill is similar to a bill of lading except that it is not negotiable. It serves as a receipt of goods by the airline company, a contract of carriage between the trader/exporter and the Airline company as well as a document of title to the goods.
14. Freight note; a document issued by the shipping company showing the amount of freight due on a shipment of goods.
15. Weight note; is a document that lists the gross weight of the packages or cases containing goods issued by the supplier to the buyer.
16. Certificate of insurance; is a statement of coverage issued by the insurance company insuring the goods.
17. Import license; is a document issued by government for the importation of certain type of goods. The purpose may be to:
    a. Limit the volume of imports.
    b. To control the importation of dangerous commodities such as firearms.
    c. To protect home infant industries.
    d. To preserve natural heritage and national traditions.
18. Export license; this is a document issued by government for the exportation of certain type of goods. The purpose may be to:

a. Limit the outflow of scarce resources, especially foodstuffs.
b. Control the exportation of dangerous goods.

19. Consignment note; this is a shipping agreement between the carrier and the consignor. It contains:
    a. The name and address of the carrier.
    b. The type and name of the ship/vehicle/plane in which the goods are to be carried.
    c. The name of the consignor.
    d. The name of the consignee.
    e. A brief description of goods sent.
    f. The number of packages sent.
    g. Time when the goods will be ready for collection.
    h. Cost of transport (freight charges).
    i. Terms and conditions of shipment.
    j. Signature of the carrier.

INTERMEDIARIES/AGENTS IN INTERNATIONAO TRADE

These are people businesses representing or acting on behalf of a business owner involved in import or export trade. The following intermediaries play an important role in import trade.

1. Import brokers; these are intermediaries who arrange deals between locally based importers and foreign exporters for a commission. The do not buy or sell the goods themselves but bring importers and exporters in close contact.
2. Import commission agents; these are intermediaries who sell goods locally on behalf of overseas suppliers/exporters. They get goods from abroad and sell them locally on behalf of overseas suppliers. They do not stand any risk and if the goods remain unsold, they can return them to the exporter at the exporter's expense. They deduct their commission from sales proceeds and remit the difference to the supplier.
3. Import merchants; these are traders who buy goods from abroad in their own names and sell them locally in order to make some profit. They resemble wholesalers in home trade.

4. Shipping and forwarding agents; these are agents who arrange for the transportation of goods in international trade.
   They also help in the completion of necessary documents and payment of customs duties.

The following agents play an important role in export trade:

1. Shipping and forwarding agents;
2. Export merchants; these are locally based traders who buy goods in the home market and sell them abroad at a profit. They relieve producers from the burden of looking for market abroad.
3. Marketing boards; these are trading organizations that buy agricultural products from farmers and export them to other countries.

PROTECTIONISM

This refers to restrictions/barrier imposed on international trade. Countries sometimes take some measures to regulate their volume of import or export trade for several reasons.

The following are the reasons for controlling import trade:

1. To protect home infant industries against competition from high quality low priced imported goods from developed industrialized nations.
2. To stop the importation of dangerous or undesirable goods that may have adverse effects on people's health.
3. To raise revenue for government in form of import duties.
4. To prevent dumping i.e. the selling of imported goods at giveaway prices in a local market. This reduces demand for locally produced goods hence killing local industries.
5. To encourage creation of employment opportunities in the country by encouraging development of local industries.
6. To reduce imported inflation by stopping or reducing importation of goods from countries suffering from inflation.
7. To improve on the country's balance of payments by reducing expenditure on imports.

8. To reduce overdependence on other countries by reducing over-reliance on imported goods thereby encouraging the development of local industries.
9. To protect and maintain a country's traditions and natural heritage that may be interfered with by imported goods.
10. To maintain health standards of the citizen by ensuring that all goods entering the country meet the set standards.
11. To retaliate against restrictions imposed by other countries against the country's exports.

TOOLS USED TO CONTROL IMPORT TRADE

The following are the measures used by governments to control the volume of imports:

1. Imposing heavy import duties; heavy import duties increase prices of imported thereby discouraging their consumption.
2. Total ban; this is total restriction on the importation of certain goods deemed dangerous for people's health.
3. Import quotas; this is refers to government fixing maximum quantities of certain goods to be imported in a given period.
4. Import license; is a document issued by government for the importation of certain type of goods. Import licenses may be issued to only a few importers or may be issued at very high rates to discourage importation.
5. Giving subsidies to local producers; these are incentives given to local producers in form of tax holidays, tax exceptions etc. to lower the costs of production of locally produced goods hence enabling them compete favorable against imported goods.
6. Currency devaluation; this refers to deliberate lowering of a country's currency against other currencies with the aim of making imported goods very expensive compared to locally produced goods hence discouraging importation.
7. Sanitary regulations; this involves government introducing medical standards that goods must meet before they are imported into the country. This applies mainly to foodstuffs and medicine.

8. Administrative controls; these are length procedures put in place to make it difficult and expensive to import goods into the country. For an importer to meet all the requirements, he will have to incur very high costs thereby making imported goods very expensive.
9. Foreign exchange control; this involves limiting the circulation of foreign exchange by releasing only small amounts of foreign exchange to a few importers to import a few goods.
10. Trade embargo/economic sanctions; this involve a country stopping all trading activities with a particular country.
11. Prepayment of import duties;

REASONS AGAINST CONTROLLING IMPORT TRADE (DISADVANTAGES OF PROTECTIONISM)

1. Over protection enables inefficient firms to remain in business due to lack of competition. Such firms produce low quality goods at very high costs.
2. Controlling imports may lead to economic retaliation where other countries also impose restrictions on the exports of the country thus reducing the country's exports.
3. High import duty imposed on raw materials will end up increasing the costs of production and prices of locally manufactured goods.
4. The protected local firms may turn out to be monopolies and end up exploiting consumers e.g. selling poor quality goods at very high prices.
5. Controlling import trade limits consumers′ choices as they are left to depend on only locally manufactured goods.
6. High import duties on essential commodities may lead to imported inflation e.g. taxes of petroleum products.

CUSTOMS AUTHORITIES

These are officers at the boarders who are charged with the following responsibilities:

1. Collecting revenue in form of import and export duties.
2. Preventing smuggling of goods into and out of the country.
3. Detecting and avoiding unauthorized goods from entering the country.

4. Compiling statistical information regarding goods entering or leaving the country.
5. Calculating duties payable on various categories of goods entering or leaving the country.
6. Ensuring that import and export regulations are followed.
7. Where dutiable goods are stored in a bonded warehouse pending payment of customs duties, the customs authorities control those goods so that they don't leave the warehouse before duty is paid.

CUSTOMS DUTIES

These are taxes imposed on goods entering or leaving the country. They are divided into two:

   a. Import duties; these are the taxes imposed on goods entering the country i.e. imports.
   b. Export duties; these are the taxes imposed on goods leaving the country i.e. exports.

DUTIABLE AND NON-DUTIABLE GOODS

a. Non-dutiable goods; are goods where there is no duty imposed on them. If there is no duty payable on the imported goods, the importer completes a *Free Goods Form*.
b. Dutiable goods; are goods on which duty is payable. If duty is payable of the goods entering the country, the importer completes an *Ex-Ship Form*.

TYPES OF CUSTOMS DUTIES

a. Advalorem duties; are taxes levied according to the value of the goods imported. A certain percentage is calculated on the invoice price.
b. Specific duties; are taxes levied according to the quantity/volume of goods imported e.g. per kilogram, liter etc.
c. Protective duties; are taxes imposed specifically for protective purposes e.g. to protect home infant industries against competition from imported goods, to protect the health of consumers by stopping the importation of harmful products.

CUSTOMS DRAWBACK

This is money refunded to an importer which he had paid in form of import duty should he re-export the imported goods within a stipulated period of time. Also, a manufacturer who imports raw materials and pays import duty on them, such import duty may be refunded to him if he exports the finished goods made out of the imported raw materials.

TRANSSHIPMENT

When goods have been imported for re-export, it is possible to transfer such goods from one ship to another without first warehousing them. This is called transshipment.

PROBLEMS FACED IN INTERNATIONAL TRADE/ FACTORS LIMITING INTERNATIONAL TRADE

a. Differences in languages; different countries use different languages which makes communication difficult.
b. Differences in currencies; different countries use different currencies. One must therefore convert his/her money in the appropriate currency for the exchange to take place.
c. Differences in weights and measures; for instance, while other countries use kilograms, others use pounds or tones.
d. Numerous laws and regulations imposed by different countries makes international trade difficult.
e. Numerous risks faced; such as loss or damage of goods in transit, selling goods on credit to importers who may fail to pay.
f. Long distances covered which increases the costs of transportation.
g. Import restrictions imposed by different countries which reduce market for exports.
h. Difficulty in finding market in a foreign country.
i. Geographical barriers such as lakes, mountains, seas etc. which make the cost of transport very high.
j. Stiff competition for market on the world market.
k. Inadequate foreign exchange by many developing countries. Countries need foreign exchange to buy goods from other countries.

l. Insecurity and political instabilities in some countries which increase risks of loss and makes transportation difficult.
m. Dumping of goods from industrialized nations into economies of developing countries thereby reducing demand for goods produced by developing countries.

DIFFERENCES BETWEEN HOME TRADE AND FOREIGN TRADE

1. Home trade takes place within the boundaries of the country while international trade takes place between countries.
2. Goods in home trade are subjected to excise duty while goods in foreign trade are subjected to customs duty.
3. The main intermediaries in home trade are the wholesalers and retailers while the main intermediaries in foreign trade are the importers and exporters.
4. Goods are home trade are advertised through the local media while goods in foreign trade advertised through international media.
5. Road and railway transport are the main means of transport used in home trade while air and water transport are main means of transport used in international trade.
6. Transactions in home trade are mainly done in the local currency while transactions in foreign trade are mainly done in foreign currencies.
7. Insurance of goods in home trade is not compulsory while goods in international trade must be insured.
8. Home trade has few risks while international trade is faced with many risks.
9. Home trade serves a small market while international trade serves a large market.
10. Home trade involves few documents/procedures while international trade involves many documents/procedures.
11. Goods in home trade are stored in private and public warehouses while goods in international trade are stored in bonded warehouses.

REGIONAL/ECONOMIC INTEGRATION

This refers to economic cooperation among countries in a region to benefit from each other. The countries in a region join together to form a trading bloc. The main aim is to encourage trade amongst themselves by removing barriers to international trade. Examples of integrations in the world include:

a. East African Community (EAC); comprised of Uganda, Kenya, Tanzania, Rwanda, Burundi and South Sudan.
b. Southern Africa Development Community (SADC); comprised of
c. Common Market for East and Southern Africa (COMESA); comprised of
d. European Union (EU); comprised of
e.
f.
g.

STAGES IN ECONOMIC INTEGRATION

1. Preferential Trade Area/Agreements (PTA); this is where countries in a region agree to give preferential treatment to member countries in the form of reduced tariffs on goods coming from member countries.
2. Free Trade Area (FTA); this is where countries in a region agree to abolish all tariffs on goods originating from member countries but each country maintaining its own tariff structure for goods coming from non-member countries.
3. Customs Union (CU); this is where countries in a region agree to abolish all barriers on goods coming from member countries and also set common tariffs for goods coming from non-member countries.
4. Common Market (CM); this is where abolish all barriers on goods from member countries, set uninform tariffs for goods coming from non-member countries and all for free movement of factors of production (capital and labour) among member countries.
5. Economic and Monetary Union; this is where countries abolish all barriers on goods coming from member countries, set uniform tariffs for goods coming from non-member countries, all for free movement of factors of production and also adopt similar fiscal and monetary policies.

There is also the use of a common currency managed by a shared central bank e.g. the Euro used by the European Union.

6. Political Federation/Union; this is the most advanced form of integration with a common government and the sovereignty of member countries is significantly reduced.

ADVANTAGES OF ECONOMIC INTEGRATION

1. Citizens of member countries have a wide variety of goods because of free movement of goods from between member countries.
2. Citizens in member countries acquire goods and services at a lower cost after tariffs are removed or lowered.
3. Promotes trade among member countries through the removal of trade barriers and the adoption of a common currency.
4. Large market of goods and services is created with the regional because of removal of all trade barriers.
5. Reduces duplication of industries within the region; if one industry established in a member country is enough to serve the entire region, it will not be necessary to set up similar industries in other member countries.
6. Attracts direct foreign investments in the region because of the increased market.
7. Integration can easily solve the problem of unemployment. This is because more employment opportunities are created due to increased investments and besides labour which is unemployed can easily seek employment in other member countries.
8. Increases the bargaining power of member countries and protects weaker members. This is so because an integration is stronger than individual countries.
9. Promotes healthy competition among producers in the region which results in improved quality and reduced prices.
10. Promotes peace and mutual understanding among member countries.
11. Increased access to funding/loans from international institutions. It is easier for a region to borrow large sums of money compared to individual countries.

12. Integration encourages specialization among member countries. Countries tend to concentrate where they have got comparative advantage over others since they can easily exchange for what they do not produce.
13. Political cooperation; integration can easily address conflicts and political instability in the region. This is a region can have significantly greater political influence than individual countries.
14. Shared common services; services like air and railway transport, telecommunication, joint research etc. could be shared among member countries hence reducing the burden of each country running its own services.

DISADVANTAGES OF ECONOMIC INTEGRATION

1. Integrations increase trade barriers against non-member countries, hence reducing trade with non-member countries.
2. Integration results in loss of tax revenue on goods originating from member countries.
3. Integration encourages over dependency on other countries which is dangerous in case the integration collapses.
4. It results in trade diversion; it forces a country to stop trading with low cost non-member countries and trade with high cost member countries.
5. National sovereignty may be undermined because member countries are required to give up some control over some policies.
6. There is likely to be uneven distribution of industries and general development in the region if member countries are not at the same level of development. This is because resources tend to move from less developed countries to more developed countries.
7. Integration encourages inefficient firms in the region to remain in business due to lack of competition from non-member countries.
8. Integration forces citizens of member countries to consume only the goods produced in the region irrespective of the quality and price.
9. Integration may result in the collapse of home infant industries that cannot compete against goods produced in the region.

CHALLENGES FACING INTEGRATIONS AMONG DEVELOPING COUNTRIES

1. Most developing countries produce almost similar products and therefore there is usually limited trade among themselves.
2. Differences in political ideologies and systems of governance hinders integrations.
3. Uneven distribution of industries and general development often resulting in misunderstandings.
4. Political instabilities in some countries hinders smooth running of trade among member countries.
5. Lack of a common unifying language that affects communication.

CONDITIONS FOR SUCCESSFUL INTEGRATION

1. Countries should be geographically near each other to avoiding goods from a member country passing through non-member countries before reaching another member country.
2. Countries should preferably be at the same level of development otherwise resources will tend to move from less developed countries to more developed countries.
3. Countries should preferably be of equal size in order for them to develop at the same rate.
4. Countries should have similar ideologies i.e. political views and methods of governance.
5. Countries should use a common currency in order to simplify transactions.
6. Countries should use a common language in order to simplify communication.

THE SIZE OF BUSINESS FIRMS

A firm is the smallest production unit which employs factors of production under one unit of control to produce goods and services e.g. a school, a clinic, agricultural firm, manufacturing plant etc.

An industry is a group of firms dealing in the production of a specific product. For instance, the soda industry in Uganda is made of Century

Bottling Company (Coca-Cola products), Crown Bottlers Limited (Pepsi-cola products), Haris International (Riham products) etc.

Firms can be categorized into small firms and large firms. The following factors are used to determine the size of business firms:

1. The size of capital employed; small firms employ a small amount of capital while large firms employ a large amount of capital.
2. The space or floor area occupied; small firms occupy a small space while large firms occupy a large space.
3. The size of market or number of customers served by customers; small firms serve a small market while large firms serve a large market.
4. The size of stock held and range of services offered; small firms usually hold small stock and offer limited services compared to large firms.
5. The number of people employed; small firms employ a few people as compared to large firms.
6. The techniques used in production; small firms use simple technology while large firms use advanced technology.
7. The number of departments involved and extent of specialization; large firm usually have many departments and practice specialization as compared to small firms.
8. The size of factors of production used.

SURVIVAL OF SMALL FIRMS (ADVANTAGES OF SMALL FIRMS)

1. Small firms are simpler to manage and can easily be managed by one person.
2. Owners of small firms can easily maintain personal contact with their customers. This is why firms offering personal services are usually small firms e.g. law firms, professional accountants etc.
3. Small firms require small amount of capital to start and run.
4. Small firms incur low operation expenses in terms of rent, labour etc.
5. Small firms usually locate close to the homes of customers and therefore help to bring goods closer to customers.
6. Small firms need small market for their survival.

7. They are flexible i.e. can easily change from one line of goods to another or from one location to another.
8. They are easy to form as they may not require complex legal procedures to start.
9. They require a small space (floor area) for operation, which is easy to obtain.
10. Stand less risk of loss in case of changes in consumers' tastes and preference.

DISADVANTAGES OF SMALL FIRMS

1. They face stiff competition from large firms that usually sell at low prices.
2. They find it difficult to access bank loans since owners usually lack security.
3. They don't enjoy economies of scale (advantages of large scale operation).
4. They are usually poorly managed because they cannot afford to employ skilled workers.
5. They usually cannot afford to advertise their goods or services to increase sales.
6. They make low profits and low sales since they serve a small market (few customers).
7. They cannot afford to pay premiums to insure their business from losses.
8. They offer limited variety of goods or services thereby limiting consumers' choices.
9. They often sell defective goods e.g. expired and poor-quality goods which affect consumers' health.
10. They tend to sell at higher prices because they often buy supplies from other intermediaries.

ECONOMIES OF SCALE

These are the advantages that are enjoyed by businesses due to large-scale production. These advantages are in form of reduced costs per unit as a result of operating on a large scale. They include:

1. Large firms can afford to buy modern equipment which would result in increased productivity hence reduced costs per unit.

2. Large firms employ many workers each performing only a small job (division of labour). This results in increased output and better-quality goods.
3. Large firms pay well their workers and provide fringe benefits to workers which motivates them to work harder.
4. Large firms can afford to carry out research into better methods of production leading to increased output and better quality.
5. Large firms can easily access loans from financial institutions because they are well known and have good security.
6. Large firms usually benefit from larger trade discounts because they buy goods in large quantities.
7. Large firms can afford to pay insurance premiums to protect the businesses from losses.
8. Large firms can afford to advertise their businesses hence increasing sales.

DISECONOMIES OF SCALE

These are the disadvantages incurred by firms operating on large scale. The disadvantages are in form of increased costs per unit as a result of operating on a large scale. They include:

1. Large firms are difficult to manage. This is because of having very many employees and the fact that owners and employees remain very far from each other.
2. Decision making tends to be slower in large firms and decisions take long to be implemented. This is because often the people who manage these businesses are not the owners.
3. Owners of large firms lack personal contact with their customers, which makes it difficult to know what the customers want.
4. Large firms have to spend a lot of money on advertising and market research in order to get enough market for their products.
5. Large firms suffer severely if there is a change in consumers' tastes and preferences.
6. Large firms require large amount of capital to start and run.

7. Large firms incur high operation expenses in terms of rent, electricity, labour etc.
8. Most large firms usually locate in large shopping areas of urban centres neglecting rural areas.
9. Large firms find it difficult to change from one line of goods to another or from one location to another.
10. Large firms are difficult to form as they require complex legal procedures.
11. Large firms require large space (floor area) which may be difficult to find.

THE GROWTH OF BUSINESS FIRMS

Business organizations grow in size. There are two forms of business growth; natural/internal growth and external growth/combinations.

NATURAL GROWTH

This is when a business grows using its own resources by applying the principle of ploughing back profits. This means reinvesting the profits into the business to expand its size. The owner may even admit partners to provide additional capital for expansion. At a later stage, it may be necessary to convert the business into a private limited company and eventually a public limited company.

EXTERNAL GROWTH (COMBINATIONS)

This is the coming together of two or more forms formerly independent, to form one large firm.

REASONS FOR BUSINESS COMBINATIONS

1. Elimination of competition in order to increase their profit margins.
2. Raise capital for business expansion; a business combination can easily raise capital for expansion.
3. Effective management; business combinations can hire experienced and qualified employees.
4. Market domination; businesses combine to dominate the entire market and create monopoly.
5. Economic instability; firms may combine to protect themselves against the effects of uncertain policies of the government.

6. Trade cycle; small firms may combine to deal with effects of depression and ensure their survival.
7. In order to capture competitor resources.
8. To cut costs and therefore increase profit margin.
9. To get multi-skilled technical staff.
10. Avoid excessive production.

FORMS OF BUSINESS COMBINATIONS

1. Consortium (temporary merger); this is the pooling of resources to performs a particular job/task such that as soon as the work is accomplished, the consortium comes to an end. For instance, Roko construction company may join Arab contractors Ltd to undertake the construction of a road and as soon as the work is completed, the consortium comes to an end.
2. Conglomerate (diversifying merger); this is where two or more firms producing totally unrelated goods merge e.g. a firm producing furniture combining with another brewing beer. The advantage is that should one line of business experience a fall in demand for its products, the business may depend on the other line.
3. Lateral combination; this takes place when two or more firms producing related goods that do not compete with each other for market combine e.g. a firm producing wine combining with that producing beer.
4. Absorption/merger; this takes place when one independent firm takes over another independent firm. The taken over firm losses its existence. The buying firm retains its entity and becomes stronger than previously e.g. Airtel took over Warid. All the assets of the absorbed firm are taken over by the absorbing firm.
5. Consolidation (complete amalgamation); this takes place when two or more firms combine and loss their entities and for a new firm. The combining firms are dissolved and a new firm is created in their place.
6. Cartel; this is the association of independent firms dealing in the same type of business to fix the amount of production, divide the market and determine the price for their products in order to create monopoly and maximize profits.

7. Trust; a consortium of independent organizations formed to limit competition by controlling the production and distribution of a product or service. The firms retain their ownerships and identities.
8. Holding company; is a company that owns controlling shares in other companies i.e. holds at least 51% shares in other companies. For instance, if MTN acquires 51% or more shares in Airtel, MTN will be called a holding company while Airtel its subsidiary. MTN acquires only controlling shares but the two companies retain their separate entities.

LINES OF COMBINATIONS

Firms combining in a similar field may either be engaged in business at the same level or at different levels.

1. Horizontal combination; this is where two or more firms producing similar goods at the same stage of production combine and form one firm e.g. Lugazi sugar works combining with Kakira sugar works.
2. Vertical combination; this is where two or more firms producing similar goods at different stages of production combine and form one firm e.g. a sugar processing factory combining with a sugar cane plantation. Vertical combinations are of two kinds:
    a. Backward vertical combination; this is where a firm at an advanced stage of production takes over another firm in the same industry at a lower stage of production e.g. a sugar processing factory taking over sugarcane plantations. In other words, the firm takes over sources of raw materials.
    b. Forward vertical combination; this is where a firm at a lower stage of production takes over another firm in the same industry at an advanced stage of production e.g. tea growers taking over a tea processing factory.

ADVANTAGES OF BUSINESS COMBINATIONS

1. Combinations do away with wasteful competition among companies, meaning there may be more chance of securing increased profits.
2. Business combinations increase operating capital thereby enabling the firms operate on large scale hence enjoying economies of scale.

3. The combined firms have large financial resources. Utilizing these resources, they would be able to produce better quality of products and services which benefit the consumers.
4. Establishment and management cost can be reduced. Operating costs can also be reduced by avoiding duplication.
5. A combined firm would be able to invest resources in research to develop new and innovative products. Consumers would be able to upgrade themselves to better products which satisfy their needs in a better way.
6. Bulk purchase of materials at reduced price is possible.
7. Stability of the price of goods is maintained due to elimination of cut-throat competition.
8. Patents possessed by one of the firms can be used by all the combined firms.
9. A combined firm can control the market in terms of pricing, level of supplies and sometimes may even enjoy monopoly power.
10. If small firms combine together, they would be able to survive even in difficult times such as recession and depression.
11. Firms combining together can pool their knowledge and experience. All the firms in the combination can benefit from a vast pool of such shared knowledge.
12. The value of the combined firm's securities would be higher. It would help the firm to raise capital much easily.
13. Firms can plan their production according to market requirements. The risk of overproduction can be reduced to a great extent.
14. Common problems faced by firms can be tackled easily if they come together. They can represent their demands to the government in a unified manner.

DISADVANTAGES OF BUSINESS COMBINATIONS

1. Business combination brings monopoly in the market, which may be harmful for the society. Monopolies might restrict output, create artificial scarcities, charge high prices and produce low quality goods.
2. Management of the company becomes difficult; combined firms may become too large which leads to problems in coordination and control.

Supervision might become difficult resulting in poor quality of products, wastage, corruption etc.

3. In large combined firms, decisions are delayed because of various levels of authority. The organization would not be able to utilize opportunities in the market place.
4. Combined firms might witness conflicts of power, differences of opinion, politics etc. which may destabilize the organization.
5. Lack of consumer choice; combined firms might try to wipe out competition and prevent the entry of new firms. They would aim to control the market. The consumers would be denied the freedom to choose from products of different manufacturers.
6. Business combination may result in over-capitalization; the firm might be using capital more than what is required. This would result in high costs and poor return to shareholders.
7. Lack of personal touch; in a small firm, the owner would personally know his customers. He would know each customer's tastes and preferences. The personal touch that is possible in small sized firms would not be possible in large combined firms. Tastes and preferences of individual customers might be ignored. It might lead to customer dissatisfaction, decline in sales and profitability.
8. Leads to inefficiency due to lack of competition. There is little or no motivation to improve quality, reduce costs, introduce new or improved products etc.
9. Elimination of small businesses; combinations result in monopolies, that use their financial strength to wipe out competition and prevent entry of new firms. They resort to cut-throat competition to eliminate competitors.
10.

TERMS AND MEANS OF PAYMENT

Terms of payment; these are the conditions under which a seller completes a sale. When a customer buys goods from the seller, he/she takes them under any of the following terms:

a. Cash terms.
b. Credit terms.

c. Instalment credit terms.

CASH TERMS

This is when a customer pays for the goods or services as soon as he/she gets them, even if payment is by cheque. The following alternatives are available under cash terms:

a. **Cash with order (CWO);** this is where the buys sends the money along with the order. This is often preferred when the buyer is new or his creditworthiness is doubted.
b. **Cash on delivery (COD);** this is where the seller collects the money from the buyer when he delivers the goods. This is commonly used when goods are sent through the post office (Mail-Order business); with the post office instructed to deliver the parcel upon payment.
c. **Spot cash;** this is where the buyer pays for the goods as he collects them from the seller's premises.
d. **Prompt cash;** this is a credit period which is 7 days or less i.e. the buyer is expected to pay for the goods in not more than seven days from the date of purchase.

Advantages of Cash Terms

1. The seller does not suffer from losses related to bad debts since there are not credit terms.
2. The seller gets cash in time which enables him to take advantage of cash discounts from his suppliers.
3. The seller's capital is not tied up in debts for a long period of time.
4. It is the most convenient method for small amounts.
5. There is no need for documentation or paperwork if goods are sold under cash terms.
6. The buyer is saved from the pressure of looking for money to pay debts.

Disadvantages of Cash Terms

1. It is very risky where large amounts of money are involved.
2. It is difficult to attract many customers if goods are sold only under cash terms.

3. The cash received on spot may easily be misused.

CREDIT TERMS

This is when a buyer takes the goods from the supplier without paying anything but settles the whole amount at once at later date. The credit period may range from seven days to one month for normal orders and from one month to three months for larger orders.

Advantages of credit terms

1. The seller is able to sell more goods under credit terms hence getting more profits.
2. Credit transactions promote social understanding between the seller and the buyer.
3. The seller makes more profits because goods tend to be more expensive under credit terms.
4. The buyer's standard of living improves when he gets goods or services on credit.
5. Salary earners can obtain their requirements and pay at the end of the month.

Disadvantages of credit terms

1. The seller's capital may be tired up in debts for a long period of time hence affecting the smooth running of the business.
2. The seller's business may collapse as a result of bad debts.
3. The seller bears additional costs of administering and collecting debts.
4. The seller's business image may be spoilt if he takes the buyer to court for not paying for the goods bought on credit.
5. The buyer pays more under credit terms than under cash terms.
6. The buyer is under pressure to look for money to pay for the goods he has bought on credit.
7. The buyer may be tempted to buy items he may not be in position to pay for.

INSTALMENT CREDIT TERMS/INSTALMENT PURCHASE TERMS

This is a system which allows the buyer to takes the goods on payment of a certain portion of the price of goods called down payment and promises pay to the remaining amount in regular instalments. The system is used to sell very expensive goods where the buyer may find it difficult to pay the whole amount at once e.g. machinery, motor vehicles etc.

Instalment credit is of two kinds; hire purchase and deferred payments.

Hire Purchase; this is a form of instalment credit where the item remains the property of the seller until the last instalment is paid. The buyer only receives possession of the goods on the day he pays down payment and ownership remains with the seller until the last instalment is paid. If the buyer fails to pay all the instalments, goods are repossessed by the seller and the already paid money is not refunded. The amount paid will be treated as hire charges for the goods.

Hire Purchase Agreement

This is a contract for the sale of goods under hire purchase terms between the seller (owner) and buyer (hirer).

a. The seller (owner) is considered to just be letting out his property to the buyer (hirer) for a fee (instalments). In other words, the goods are simply on hire until the last instalment is paid.
b. The buyer (hirer) is considered to just be hiring the goods until the last instalment is paid.

The Hire Purchase Agreement contains:

i. The total cost of the goods.
ii. The down payment paid at the time the buyer possesses the goods.
iii. The amount of regular instalments to be made by the buyer.
iv. A full description of the goods sold.
v. A statement that the buyer will not change title to the goods until the last instalment is paid.

Deferred payments; this is a form of instalment credit where the item becomes the property of the buyer on payment of down payment. The buyer receives both possession and ownership of the goods on the day he pays

down payment. The seller cannot repossess the goods when the buyer fails to pay all the instalment. He can only take legal action to recover the unpaid amount.

ADVANTAGES OF INSTALMENT CREDIT

To the seller:

1. The seller is able to sell more goods under instalment credit terms hence increasing his profits.
2. As buyers frequent the shop to pay their instalments, they may be attracted to buy more goods under similar terms.
3. The method promotes social understanding between the seller and the buyer.
4. The seller gets more profits because goods tend to be more expensive under credit terms.
5. The seller can repossess the goods sold under hire purchase if the buyer fails to pay all the instalments.
6. The seller's market expands (attracts new buyers) because customers find this system convenient to them.
7. The seller is provided with continuous working capital when he has a large number of buyers paying their instalments throughout the year.
8. The hire purchase interest constitutes addition profits for the seller.

To the buyer:

1. The buyer enjoys the use of the goods while he is still paying for them.
2. The system enables people to acquire expensive items since payment is spread over a long period of time.
3. The buyer is given time to look for money to pay the instalments.
4. The item bought may be used to make money and then pay for itself e.g. a motorcycle may be used for boda-boda.
5. The buyer's standard of living improves when he acquires expensive items.
6. The buyer is encouraged to save in terms of assets/property.
7. The item bought may be used as security to acquire loans from banks.

8. The buyer can afford to buyer other items since he does not spend all the money on one item.

DISADVANTAGES OF INSTALMENT CREDIT

To the seller:

1. Under deferred payments, the seller cannot repossess the goods in case the buyer fails to pay all the instalments.
2. At times the item repossessed may be badly damaged so that it cannot be resold to recover the remaining amount.
3. The seller's capital is tire up in debts for a long period of time thereby affecting the business.
4. The system calls for proper keeping of records which is expensive.
5. The seller suffers in case of a fatal accident to the item like cars where even the buyer dies.
6. Taking the buyer to court for failing to pay all the instalments may spoil the image of the business i.e. it may discourage other customers form buying the seller's goods.
7. Selling goods under instalment credit requires a lot of capital.
8. The seller incurs additional cost of administering and collecting debts.

To the buyer:

1. Goods under instalment credit tend to be more expensive compared when sold under cash terms.
2. The buyer may be tempted to acquire items he cannot afford to pay for.
3. Under hire purchase, the buyer loses the goods if he does not pay all the instalments.
4. The down payment is often too high for some buyers.
5.

MEANS OF PAYMENT

These are the main ways by which debts are settled. The principal channels through which debts are settled include:

1. Cash; this consists of the use of currency notes and coins issued by the central bank. It is the most common method of settling debts especially those involving small amounts of money.
2. The Post Office also provides mean of remitting (sending) money e.g. postal orders, money orders, telegraphic money orders, postage stamps, registered post etc.
3. Commercial banks provide several means of payments e.g. cheques, bank drafts, credit cards, debit cards, credit transfers, standing order payments, travelers cheques, direct debits etc.
4. Mobile telecommunication companies such as MTN, Airtel etc. also provide means of payment and remitting money e.g. MTN mobile money.
5. Businessmen also provide several instruments of credit, which are written promises to make payments in the future e.g. bills of exchange, promissory notes, I owe You etc.

ADVANTAGES OF PAYING BY CASH

1. It is the most convenient method of payment for small debts.
2. Currency notes and coins are legal tender and are therefore readily acceptable in settlement of debts.
3. Cash is always ready for use the moment it is received, unlike cheques that have to be taken for collection.
4. Cash payments are completed on spot without wasting time.

DISADVANTAGES OF PAYING BY CASH

1. It is very risky where large amounts of money are involved.
2. Currency notes and coins are only accepted in the countries of issue.
3. Counting a large number of currency notes and coins is very tiresome and time consuming.
4. Cash can be very heavy and bulk and therefore not convenient to carry about.
5. People without cash on hand cannot buy goods.
6. Payments by cash leave behind no record for future reference unless a receipt is issued.

7. It is possible to make mistakes when counting large number of currency notes and coins.
8. Payments by cash can be delayed due to lack of change especially when making small payments.

PAYING THROUGH THE POST OFFICE

The post office does not provide means of payment in the real sense, but merely means of remitting (sending) money at a small fee.

Disadvantages of paying through the Post Office

1. Paying through the post office is very slow compared to electronic means like mobile money.
2. It requires both the sender and receiver to physically go to the post office to send and receive money.

REGISTERED POST

This is a post office facility that guarantees safe delivery of documents and valuable items such as cash, bank drafts, land titles etc. the post office undertakes to compensate the sender if the parcel gets lost due the negligence of the post office officials. The post office supplies special envelopes for sending registered mail, although ordinary envelopes may also be used. The commission charged depends on the amount sent.

The letter is registered at the post office and a certificate of posting (receipt) is issued to the sender. The sender uses this document when claiming for compensation in case the letter gets lost.

Registered letters are not delivered through the post box of the addressee, instead a note is put in his box informing him of the arrival of a registered mail. He must produce this note at the counter and prove his identity when claiming for the parcel. This eliminates the possibility of the envelope landing into wrong hands.

POSTAL ORDERS

These are cards sold by the post office, that one can buy and send to another person so that he can exchange them for cash. They are sold in different

denominations of shs10,000, shs20,000, shs50,000 etc. and are payable at any post office within the country of issue. The sender buys the postal orders from any post office plus a small fee called poundage. He writes the name of the payee on the face and then send them to him in a registered mail. If they are crossed, payment will be made only through the bank account of the payee.

Advantages of postal orders

1. There is no need for a bank account for both the sender and the payee.
2. Postal orders are payable at any post office within the country of issue.
3. Postal orders cannot bounce since they are already paid for by the sender.
4. Postal orders can be crossed such that the money is paid through the bank account of the payee.
5. They are sold in different denominations of shs10,000, shs20,000, shs50,000 etc.
6. They are sold in different currencies.

Disadvantages of postal orders

1. Postal orders are a slower means of remitting money compared to electronic means.
2. Requires both the sender and receiver to physically move to the nearest post office.
3. Postal orders are not negotiable i.e. only the payee named on its face can collect the money.
4. Postal orders provide no proof of payment which increases chases of disputes.

MONEY ORDERS

A money order is a financial instrument that you can buy at a post office and send to somebody so that he can exchange it for money. The sending posting office instructs the paying post office to pay a named payee. It is mainly used when remitting large sums of money.

The sender fills an application form, which he hands over to a post office official together with the money to be sent. The official writes out the order and is sent to the paying post office to pay the named payee.

The sender is issued with a receipt which he sends to the payee in a separate envelope. On receipt of the money order receipt, the payee approaches the paying post office to claim for the money. He is required to prove his identity and also to disclose the name of the sender. A higher poundage is charged for sending money orders as compared to sending postal orders.

Advantages of money orders

1. There is no need for a bank account for both the sender and the payee.
2. Money orders cannot bounce since they are already paid for by the sender.
3. Money orders are a much safer means of remitting money through the post office.
4. There is less risk of theft compared to sending cash.
5. Money orders provide proof of payment, which eliminates disputes.

Disadvantages of money orders

1. Money orders are a slower means of remitting money compared to electronic means.
2. Requires both the sender and receiver to physically move to the nearest post office.
3. Money orders are not negotiable i.e. only the payee named on its face can collect the money.
4. Money orders can only be paid at the named post office.

TELEGRAPHIC MONEY ORDERS

This is a post office facility for sending money in case of an emergency. The money order is sent in form of a telegram to the paying post office and a copy of the telegram is immediately placed in the payee's post box. The payee produces the telegram and proves his identity when claiming for the money. A higher poundage is paid for sending a telegraphic money order compared to an ordinary money order.

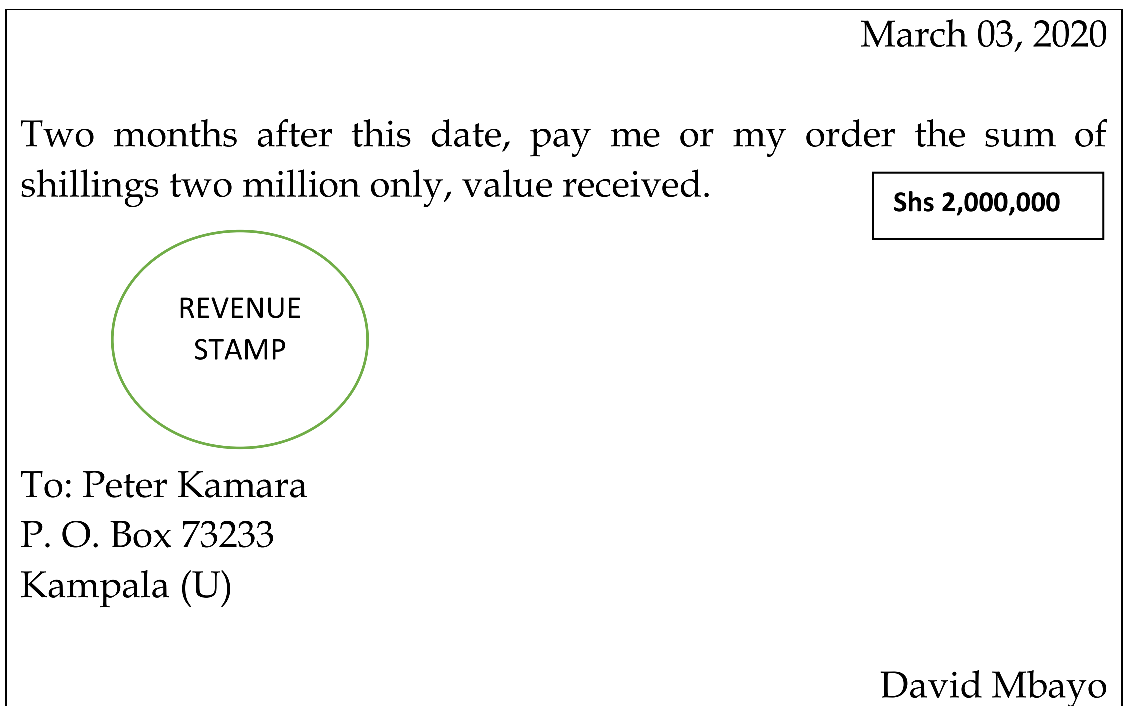
POSTAGE STAMPS

Postage stamps can be used in settlement of very small debts. The postage stamps so received will then be used for sending letters.

INSTRUMENTS OF CREDIT ISSUED BY BUSINESSES

BILLS OF EXCHANGE

A bill of exchange is an unconditional order in writing by a creditor to a debtor, requiring the person to whom it is addressed to pay on demand or at a stated future date, a sum of money to a named person or his order or the bearer. Example



March 03, 2020

Two months after this date, pay me or my order the sum of shillings two million only, value received.

Shs 2,000,000

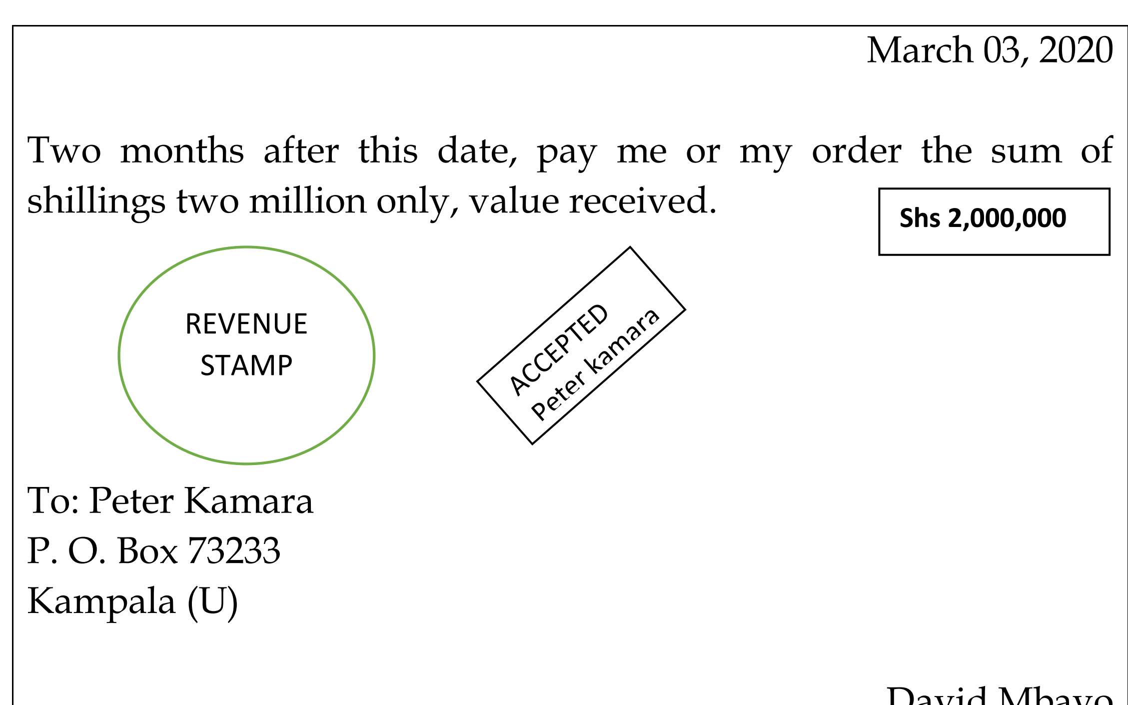
REVENUE STAMP

To: Peter Kamara
P. O. Box 73233
Kampala (U)

David Mbayo

ACCEPTANCE

This is the act of writing the word 'Accepted' across the face of the bill by the drawee and signing his name. Before a bill of exchange is accepted, it is called a draft. After acceptance, a bill of exchange becomes legally enforceable.



March 03, 2020

Two months after this date, pay me or my order the sum of shillings two million only, value received.

Shs 2,000,000

REVENUE STAMP

ACCEPTED
Peter kamara

To: Peter Kamara
P. O. Box 73233
Kampala (U)

David Mbayo

Essentials of a bill of exchange

A bill of exchange must

a. Be signed by the drawer.
b. Must be accepted by the drawee.
c. Be unconditional.
d. Bear the appropriate revenue stamps.
e. Have the amount of money demanded both in words and figures.
f. Dated i.e. bear the date when it was drawn.
g. Have the name of the drawer and drawee.

Parties to a bill of exchange

a. **Drawer;** this is the person who writes a bill of exchange to demand payment. In the above case, the drawer is David Mbayo.
b. **Drawee;** this is the person to whom the bill is addressed i.e. the person demanded money. In the above case, the drawee is Peter Kamara.

c. **Acceptor;** this is the person who writes the word 'Accepted' across the face of the bill and signs his name. A bill of exchange is accepted by the drawee. In the above case, the drawee is Peter Kamara.
d. **Payee;** this is the person to whom the money is to be paid. The payee is named by the drawer, but quite often, the drawer names himself as the payee. In the above case, the payee is David Mbayo.

ENDORSEMENT OF A BILL OF EXCHANGE

Once a bill of exchange has been accepted by the drawee, the drawer can either:

a. Keep it until the maturity date and present it to the drawee for payment, or
b. Endorse it to transfer payment to another person or discount it with a money lending institution to get money before the maturity date.

Endorsement is the act of signing on the back of the bill by the drawer/ current payee to transfer payment to another person. This is because a bill of exchange is also payable to the order of the drawer/current payee i.e. any other person to whom the drawer/current payee may wish to transfer payment to.

Types of Endorsement

a. **Open endorsement;** this is where the drawer/current payee signs his/ her name on the back of the bill without naming the new payee. A bill endorsed in such a way becomes payable to the bearer i.e. the person who presents it to the drawee. The person receiving such a bill can either insert his name as the new payee or insert someone else's name if he wishes to pass the bill on.
b. **Special endorsement;** this is where the drawer/current payee signs his/her name on the back of the bill and names the new payee.
c. **Conditional endorsement;** this involves the endorser stating one or more conditions which must be fulfilled before the new payee assumes the right to get money against the bill.

Endorser; this is the person who signs on the back of a bill to transfer payment to another person.

Endorsee; this is the person in whose favor a bill has been endorsed. The current endorsee becomes the new payee.

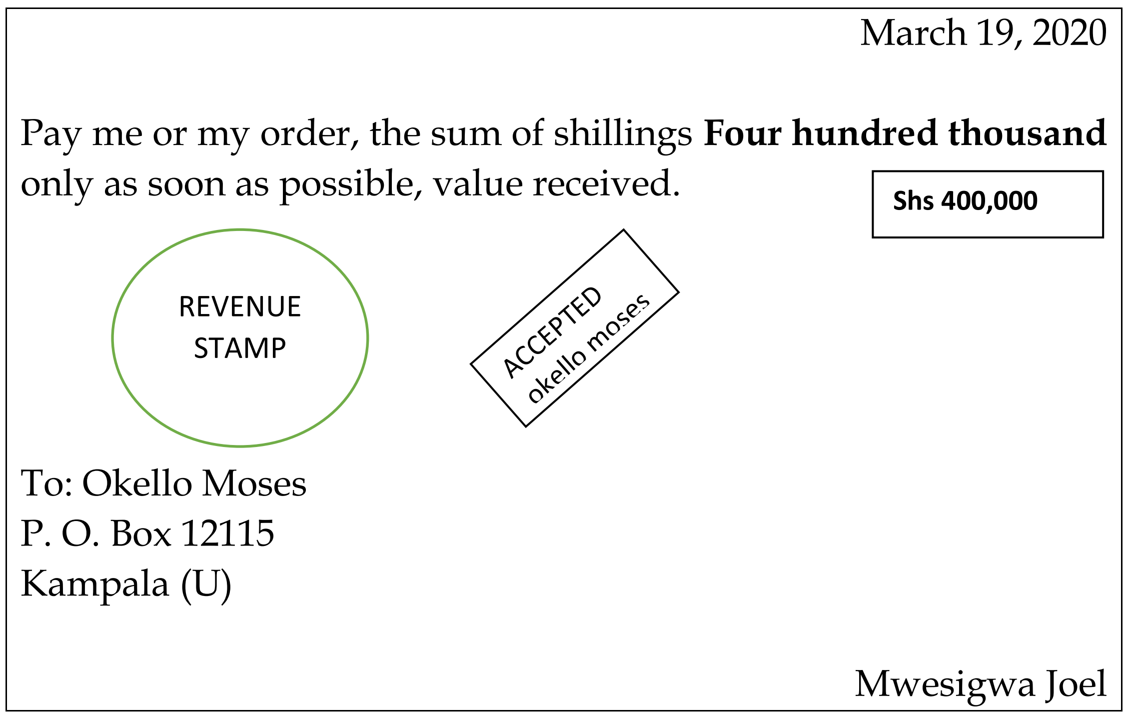
DISCOUNTING A BILL OF EXCHANGE

This is when the drawer/current payee endorses the bill to a money lending institution, which pays him the value of the bill less interest for the unexpired period. The interest deducted is called a discount.

NB: Discount houses are special institutions that specialize in lending money against bills of exchange.

SIGHT AND USANCE BILLS

A sight bill is a bill of exchange payable on demand. See example bellow:



March 19, 2020

Pay me or my order, the sum of shillings **Four hundred thousand** only as soon as possible, value received.

Shs 400,000

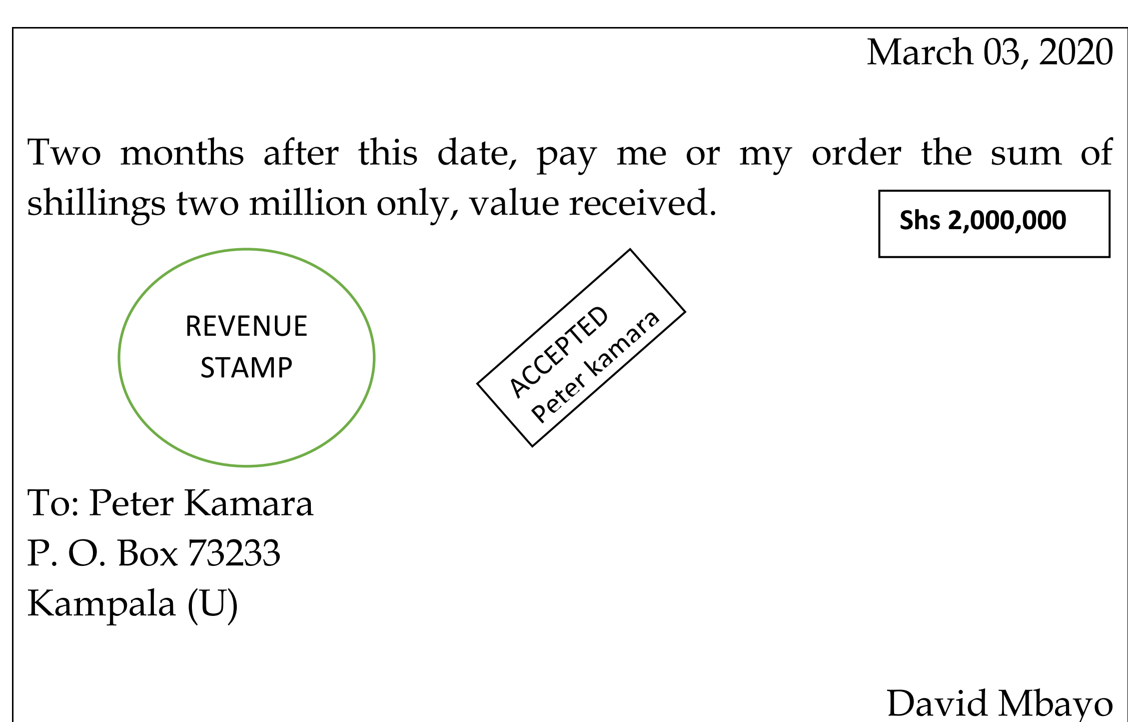
REVENUE STAMP

ACCEPTED
okello moses

To: Okello Moses
P. O. Box 12115
Kampala (U)

Mwesigwa Joel

Usance bill; this is a bill of exchange payable at a future date. See example bellow:



March 03, 2020

Two months after this date, pay me or my order the sum of shillings two million only, value received.

Shs 2,000,000

REVENUE STAMP

ACCEPTED
Peter kamara

To: Peter Kamara
P. O. Box 73233
Kampala (U)

David Mbayo

The above bill is payable two months from the date on which it was drawn i.e. the drawee (Peter Kamara) is required to pay the amount of the bill on May 03, 2020. This date is called the maturity date.

Usually three days are allowed after this date to allow the drawee to make arrangements for payment. These three days are called the days of grace.

HOLDER IN DUE COURSE

This is the person who holds the bill of exchange before it becomes due for payment. He is the last person in whose favor a bill has been endorsed.

TENURE OF A BILL

This is the time when a bill is drawn up to its maturity. The tenure of the above bill is two months.

BEARER BILL

This is a bill of exchange in which the drawer has named no payee. It becomes payable to anybody holding it i.e. the bearer.

HONOURING AND DISHONOURING A BILL OF EXCHANGE

When the drawee pays the amount against the bill on its maturity, he is said to have honoured the bill. A bill of exchange which is honoured before its maturity date is called a retired bill.

If the drawee fails to pay the amount of the bill on its maturity, the bill will be said to have been dishonoured. In this case, the drawer may extend the maturity date or take legal action to recover the money.

Conditions under which a bill may be dishoured:

1. If the drawee is bankrupt.
2. If the drawee dies.
3. If the drawee becomes insane.
4. If the bill was not signed by the drawer.
5. If much money is included on the bill than what the drawee owes.

LIABILITY UNDER AN ENDORSEMENT

Should a bill of exchange be dishonoured after it has been endorsed, the last endorsee has the right to recover the money from or take legal action against any of the endorsers and the drawee. But the ultimate liability rests with the drawee who accepted the bill.

TYPES OF BILLS OF EXCHANGE

1. **Trade bill;** this is a bill of exchange resulting from a trading activity i.e. the drawee is required to pay for the goods bought by him. Most bills of exchange are trade bills.
2. **Accommodation bill;** this is a bill of exchange which is accepted not for value received. It is simply a form of guarantee by the drawee to enable the drawer get money from a financial institution against a bill of exchange. A businessperson who finds himself short of money may get a reputable person to accept a bill of exchange drawn by him. He can then discount the bill with a financial institution and get ready cash against it.

When the bill matures, he (drawer) pays the amount direct to the discounting bank. The drawee is simply a guarantor.

3. **Inland bill;** is a bill of exchange where both the drawer and drawee are from the same country.
4. **Foreign bill;** is a bill of exchange whose drawer and drawee are from different countries.

   NB: inland bills are used in home trade while foreign bills are used in international trade.

Advantages of bill of exchange

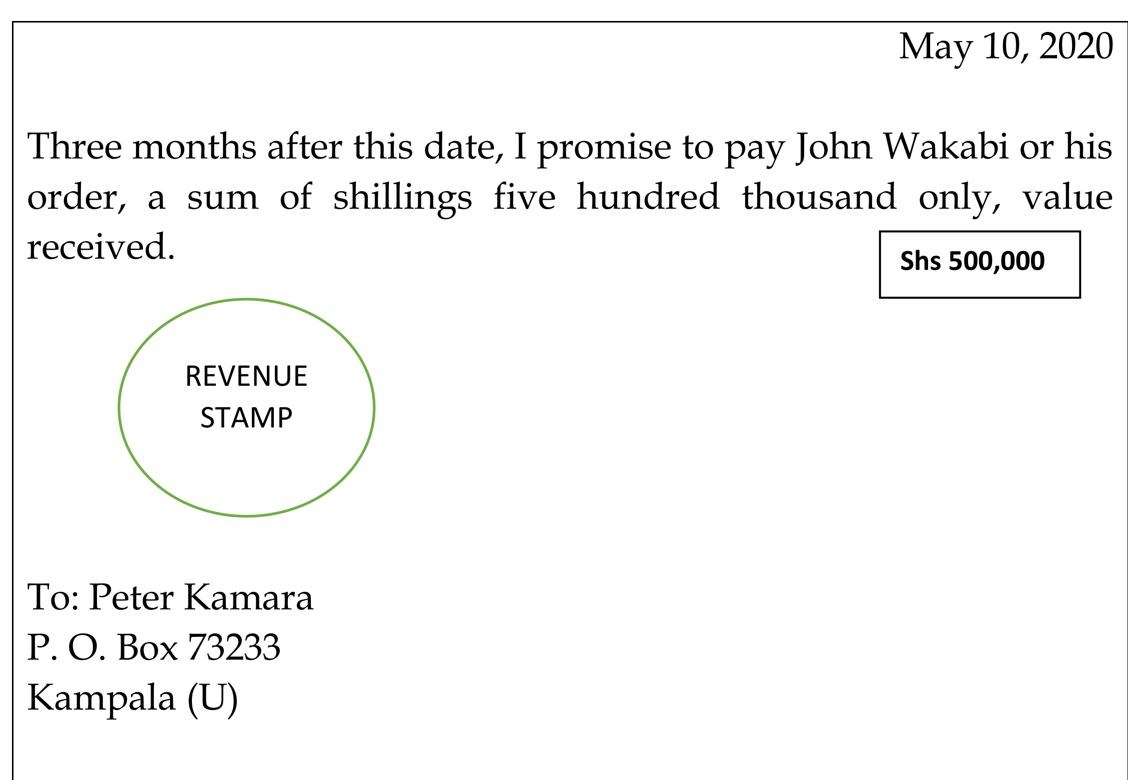
1. It serves as evidence of a debt and can be used in courts of law in case to drawee fails to pay.
2. Since the date of payment is fixed, the debtor/drawee knows when he is required to pay and the creditor/drawer knows when to expect the money.
3. Since it is negotiable, it can easily be transferred in settlement of debts.
4. If the drawer is in need of money before the maturity date, the bill can be discounted with a financial institution.
5. A bill of exchange enables the buyer to buy goods on credit and pay after the period of credit.
6. If facilitates movement of capital since it is an instrument of credit.

Disadvantages of bills of exchange

1. A bill of exchange is liable to be dishonored by the drawee.
2. Banks discount bills only that they are fully satisfied with the credibility of the holder and the drawer.
3. When the holder loses the bill, he also loses the money.

PROMISSORY NOTES

This is a written promise by a debtor to a creditor, to pay him or his order a stated amount of money before a particular date.



May 10, 2020

Three months after this date, I promise to pay John Wakabi or his order, a sum of shillings five hundred thousand only, value received.

Shs 500,000

REVENUE STAMP

To: Peter Kamara
P. O. Box 73233
Kampala (U)

David Mbayo

Promissory notes are mainly used by money lending institutions which ask their debtors to sign promissory notes when advancing loans to them. The lender may either keep it until the maturity date and then present it to the drawer for payment or may endorse it to transfer payment to someone else or discount it with a financial institution before maturity.

Parties to a promissory note

a. **Promisor/drawer;** this is the person who owes money and promises to pay i.e. debtor.
b. **Promisee/Drawee;** this the person to whom the promise of payment is made i.e. creditor.

Similarities between bills of exchange and promissory notes

a. Both are instruments of credit i.e. give evidence of a debt.
b. Both are negotiable i.e. may be endorsed or discounted before maturity date.

Differences between bills of exchange and promissory notes

a. A promissory note is drawn and signed by a person who owes money (debtor) while a bill of exchange is drawn and signed by a person demanding payment (creditor).
b. A promissory note does not need any acceptance while a bill of exchange must be accepted by the drawee to become legally enforceable.
c. A promissory note is simply a promise by a person to pay while a bill of exchange is an order/demand to a person to pay.
d. In the case of a promissory note, it is the drawer liable to pay while for a bill of exchange, it is the drawee supposed to pay.

I OWE YOU (IOU)

Like a promissory note, this is drawn by the debtor to the creditor indicating that some amount of money is owed to the creditor.

June 22, 2020

To Moses Kambedha
I owe you shillings five million only.

James Kakooza

NEGOTIABLE INSTRUMENTS

These are documents whose title can eeasily be transferred from one peron to another either by simple delivery of the document or by endorsement e.g. bills of exchange, promissory notes, cheques, bills of lading etc.

Features of negotiable instruments

a. They entitle the holder to receive a certain sum of money.
b. Title to the document can be transferred from one person to another by endorsement.

c. They can be discounted to a financial institution before the maturity date.
d. A person holding it cannot have a better title to the document than the person who gave it to him had.

Advantages of negotiable instruments

a. They can be used as security to obtain property or money.
b. They can easily be transferred from one person to another by endorsement.
c. They can be discounted before maturity date so that the holder gets cash to run his business.